

# University of Miami Law Review

---

Volume 8  
Number 4 *Miami Law Quarterly*

Article 18

---

7-1-1954

## Corporations – Share Dividends – Principal or Income?

Alan H. Dombrowsky

Follow this and additional works at: <https://repository.law.miami.edu/umlr>

---

### Recommended Citation

Alan H. Dombrowsky, *Corporations -- Share Dividends -- Principal or Income?*, 8 U. Miami L. Rev. 646 (1954)

Available at: <https://repository.law.miami.edu/umlr/vol8/iss4/18>

This Case Note is brought to you for free and open access by the Journals at University of Miami School of Law Institutional Repository. It has been accepted for inclusion in University of Miami Law Review by an authorized editor of University of Miami School of Law Institutional Repository. For more information, please contact [library@law.miami.edu](mailto:library@law.miami.edu).

## CORPORATIONS—SHARE DIVIDENDS— PRINCIPAL OR INCOME?

Plaintiffs claim that share dividends on shares specifically bequeathed in decedent's will are within the specific bequest and do not fall into the residuary clause as property acquired after execution of the will. *Held*, share dividends amount only to a dilution of original shares and are a change in form and not in substance, therefore bequeathment of original shares was held to act on all subsequent share dividends. *In re Vail's Estate*, 67 So.2d 665 (Fla. 1953).

Suit for specific performance by plaintiff corporation to recover stock paid as a dividend to the defendant under an agreement that the defendant's ownership was restricted to his period of employment, without right of transfer or assignment. Administrator claims defendant's ownership of dividend stock, under the aforementioned agreement that cash dividends were owned by the defendant. *Held*, defendant did not gain ownership of the share dividend, he merely received the right to cash dividends thereon. Share dividend represented only a dilution of defendant's original holding of corporate stock. *W. O. Barnes Co., Inc., v. Folsinski*, 60 N.W.2d 302 (Mich. 1953).

Do dividends payable in shares of stock constitute income or principal? This question has been resolved by courts via the Pennsylvania rule, the Massachusetts rule, and the Kentucky rule.<sup>1</sup>

The Kentucky rule states, in effect, that all dividends, cash or shares will be treated as income,<sup>2</sup> contending that any other view would inflict a hardship on the life tenant to whom the income is due.<sup>3</sup> This can be avoided by a clear expression of intention by the testator.<sup>4</sup> The Kentucky rule represents a minority view.<sup>5</sup>

The Pennsylvania, or American rule states that share dividends will be applied to principal in an amount necessary to maintain its value intact;<sup>6</sup> the balance of the dividend will be deemed profit.<sup>7</sup> The fact

---

1. 12 FLETCHER, CORPORATIONS §§ 5397, 5398, 5400 (Rev. & Perm. ed. 1932).

2. *Robinson v. Robinson*, 221 Ky. 245, 298 S.W. 701 (1927); *Goff v. Evans*, 217 Ky. 664, 290 S.W. 490 (1927).

3. *Hite v. Hite*, 93 Ky. 257, 20 S.W. 778 (1892).

4. *Laurent v. Randolph*, 306 Ky. 134, 206 S.W.2d 480 (1947).

5. 12 FLETCHER, CORPORATIONS § 5400 (Rev. & Perm. ed. 1932).

6. *Earp's Appeal*, 28 Pa. 368 (1857).

7. *Heard v. Bank of Am. Nat. Trust and Saving Ass'n*, 107 Cal. App.2d 225, 236 P.2d 810 (1951); *Heyn v. Fidelity Trust Co.*, 174 Md. 639, 1 A.2d 83 (1938); *Goodwin v. McGaughey*, 108 Minn. 247, 122 N.W. 6 (1909); *Sperry's Estate v. Sperry*, 189 Miss. 321, 196 So. 653 (1940); *Re Davis*, 127 Misc. 701, 217 N.Y. Supp. 605 (Surr. Ct. 1926); *Went's Estate*, 12 Pa. D. & C. 398 (1929); *Waterman's Estate*, 279 Pa. 491, 124 Atl. 166 (1924); *Nashville Trust Co. v. Tyne*, 194 Tenn. 435, 250 S.W.2d 937 (1952); *Heaton's Estate*, 89 Vt. 550, 96 Atl. 21 (1915); *Boyle's Estate*, 235 Wis. 591, 294 N.W. 29 (1940).

that a dividend is in cash or shares makes little difference as to whether it is principal or income.<sup>8</sup> The burden of proof as to a diminution of value in the principal is on the trustee, subject to review by court.<sup>9</sup> The value is ascertained as of the time the trust began,<sup>10</sup> all capital losses are subtracted from this value.<sup>11</sup> The rule does not apply if the parties clearly express their intention.<sup>12</sup> The Pennsylvania rule was subsequently abolished by statute in Pennsylvania<sup>13</sup> and New York.<sup>14</sup> The statute was not retroactive<sup>15</sup> and the Pennsylvania rule applies to wills enacted before the statute was in force.<sup>16</sup>

The Massachusetts rule holds that all share dividends, in shares of the issuing corporation,<sup>17</sup> are a dilution of capital,<sup>18</sup> regardless of the period of accumulation,<sup>19</sup> and go to the principal.<sup>20</sup> Share dividends in stock of another corporation are treated as cash dividends.<sup>21</sup> One court has construed "dividend" in a will that stated "income or dividends" to mean cash dividends and not share dividends.<sup>22</sup> A clear manifestation of the intention of the parties will avoid application of the rule.<sup>23</sup>

United States' courts define share dividends as ones in which the stockholder's interest in the corporation remains unchanged upon receipt of the share dividends.<sup>24</sup> An increase in interest represents income rather

8. *Holbrook v. Holbrook*, 74 N.H. 201, 66 Atl. 124 (1907).

9. *Heard v. Bank of Am. Nat. Trust and Savings Ass'n*, 107 Cal. App.2d 225, 236 P.2d 810 (1951); *Re Waterhouse's Estate*, 308 Pa. 422, 162 Atl. 295 (1932).

10. *Wittmer's Estate*, 283 Pa. 311, 129 Atl. 85 (1925).

11. *Dickinson's Estate*, 285 Pa. 449, 132 Atl. 352 (1926).

12. *Jackson v. Jackson*, 22 N.J. Super. 269, 91 A.2d 892 (Ch. 1952); *Central Hanover Bank and Trust Co. v. Bruns*, 16 N.J. Super. 199, 84 A.2d 475 (Ch. 1951); *Re Osborne*, 209 N.Y. 450, 103 N.E. 723 (1913); *Flaccus' Estate*, 283 Pa. 185, 129 Atl. 74 (1925).

13. PA. STAT. tit. 20, § 3470.5 (1945).

14. N.Y. PERS. PROP. LAWS § 17-a.

15. *Crawford's Estate*, 362 Pa. 458, 67 A.2d 124 (1949).

16. *Strong's Will*, 203 Misc. 1060, 118 N.Y.S.2d 810 (Surr. Ct. 1952); *King's Estate*, 361 Pa. 629, 66 A.2d 68 (1949).

17. *Old Colony Trust Co. v. Jameson*, 256 Mass. 179, 152 N.E. 52 (1926).

18. *Williams v. Western Union Tel. Co.*, 93 N.Y. 162 (1833).

19. *Buder v. Franz*, 27 F.2d 101 (9th Cir. 1928).

20. *Lanston v. Lanston*, 290 Fed. 315 (D.C. Cir. 1923); *First Nat. Bank of Tuscaloosa v. Hill*, 241 Ala. 606, 4 So.2d 170 (1941); *Armstrong v. Merts*, 202 Ga. 483, 43 S.E. 2d 512 (1947); *McHenry v. McHenry*, 152 Ga. 105, 108 S.E. 522 (1921); *Burns v. Hines*, 298 Ill. App. 563, 19 N.E.2d 383 (1939); *Rand v. Hubbel*, 115 Mass. 461 (1874); *Minot v. Paine*, 99 Mass. 101 (1868); *Joy's Estate*, 247 Mich. 418, 225 N.W. 878 (1929); *MacKellar v. Stebbins*, 244 Mich. 170, 221 N.W. 275 (1928); *Wachovia Bank and Trust v. Jones*, 210 N.C. 339, 186 S.E. 335 (1936); *Lamb v. Lehman*, 110 Ohio St. 59, 143 N.E. 276 (1924); *Kirby v. Western Surety Co.*, 68 S.D. 612, 5 N.W.2d 405 (1942).

21. *Old Colony Trust Co. v. Jameson*, 256 Mass. 179, 152 N.E. 52 (1926).

22. *Fifth-Third Union Trust Co. v. Davis*, 55 Ohio App. 377, 10 N.E. 4 (1936).

23. *Equitable Trust Co. v. Prentice*, 223 App. Div. 615, 229 N.Y. Supp. 250 (1st Dep't 1928); *Macy v. Ladd*, 128 Misc. 732, 219 N.Y. Supp. 449 (Sup. Ct. 1926); *DeWeese v. Piqua Memorial Hospital Ass'n*, 85 Ohio App. 310, 82 N.E.2d 870 (1948); *Re Dittmer*, 197 Wis. 304, 222 N.W. 323 (1928).

24. *Koshland v. Helvering*, 298 U.S. 441 (1936); *Commissioner of Internal Revenue v. Tillotson Mfg. Co.*, 76 F.2d 189 (6th Cir. 1935); *Michaels v. McLaughton*, 20 F.2d 959 (N.D. Cal. 1927).

than principal.<sup>25</sup> A share dividend does not constitute income to the stockholder.<sup>26</sup> Unauthorized share dividends are treated as cash dividends.<sup>27</sup>

The court in the *Folsinski*<sup>28</sup> case cites *In re Joy's Estate*,<sup>29</sup> in which the Michigan court adopted the Massachusetts rule, holding that share dividends are applied to principal and are not income.<sup>30</sup> The Florida court in *In re Vail's Estate*<sup>31</sup> adopted the theory of *Williams v. Western Union Telegraph Co.*,<sup>32</sup> in which Justice Cardozo stated, "A stock dividend does not distribute property but simply dilutes the shares as they existed before."<sup>33</sup> Florida, in adhering to this view, rendered the decision on what would be an application of the Massachusetts rule.

The Massachusetts rule, as applied by the courts of Michigan and Florida in the instant cases, represents the adoption of a rule of convenience that will not impose the burden on the trustee of a complex disbursement system of dividends received. The courts have hereby given the trustee a plain principle to guide him.

Alan H. Dombrowsky

## FEDERAL COURTS—FOREIGN AID APPROPRIATIONS ACT—SURVIVAL OF FEDERAL COMMON LAW

Performance of a contract to purchase manufactured printing presses destined for export to Russia was refused by vendee on the ground that an export license could not be obtained. Vendor subsequently sold the goods to the United States at a profit, and vendee brought suit to recover the down-payment on the contract price. On appeal from a district court decision for defendant-vendor,<sup>1</sup> *held*, reversed. The plaintiff-vendee was entitled to restitution of the down-payment beyond and above any injury suffered by defendant, where an export license had been refused by the United States, on the ground that national public policy as promulgated by Congress in the Foreign Aid Appropriations Act<sup>2</sup> required such a rule. *Amtorg Trading Corp. v. Miehle Printing Press & Mfg. Co.*, 206 F.2d 103 (2d Cir. 1953).

25. *Bass v. Commissioner of Internal Revenue*, 129 F.2d 300 (1st Cir. 1942); *Strassburger v. Commissioner of Internal Revenue*, 124 F.2d 315 (2d Cir. 1941); *Helms Bakeries v. Commissioner of Internal Revenue*, 46 B.T.A. 308 (1942).

26. *Helvering v. Griffiths*, 318 U.S. 371 (1943); *Eisner v. Mancomber*, 252 U.S. 189 (1920); *Towne v. Eisner*, 245 U.S. 418 (1918).

27. *Vogt Mach. Co. v. United States*, 39 F.2d 986 (Ct. Cl. 1930).

28. 60 N.W.2d 302 (Mich. 1953).

29. 247 Mich. 418, 225 N.W. 878 (1929).

30. *Minot v. Paine*, 99 Mass. 101 (1868).

31. 67 So.2d 665 (Fla. 1953).

32. 93 N.Y. 162 (1883).

33. *Williams v. Western Union Tel. Co.*, 93 N.Y. 162, 189 (1883).

1. 108 F. Supp. 170 (S.D. N.Y. 1952).

2. 62 STAT. 1054 (1949).